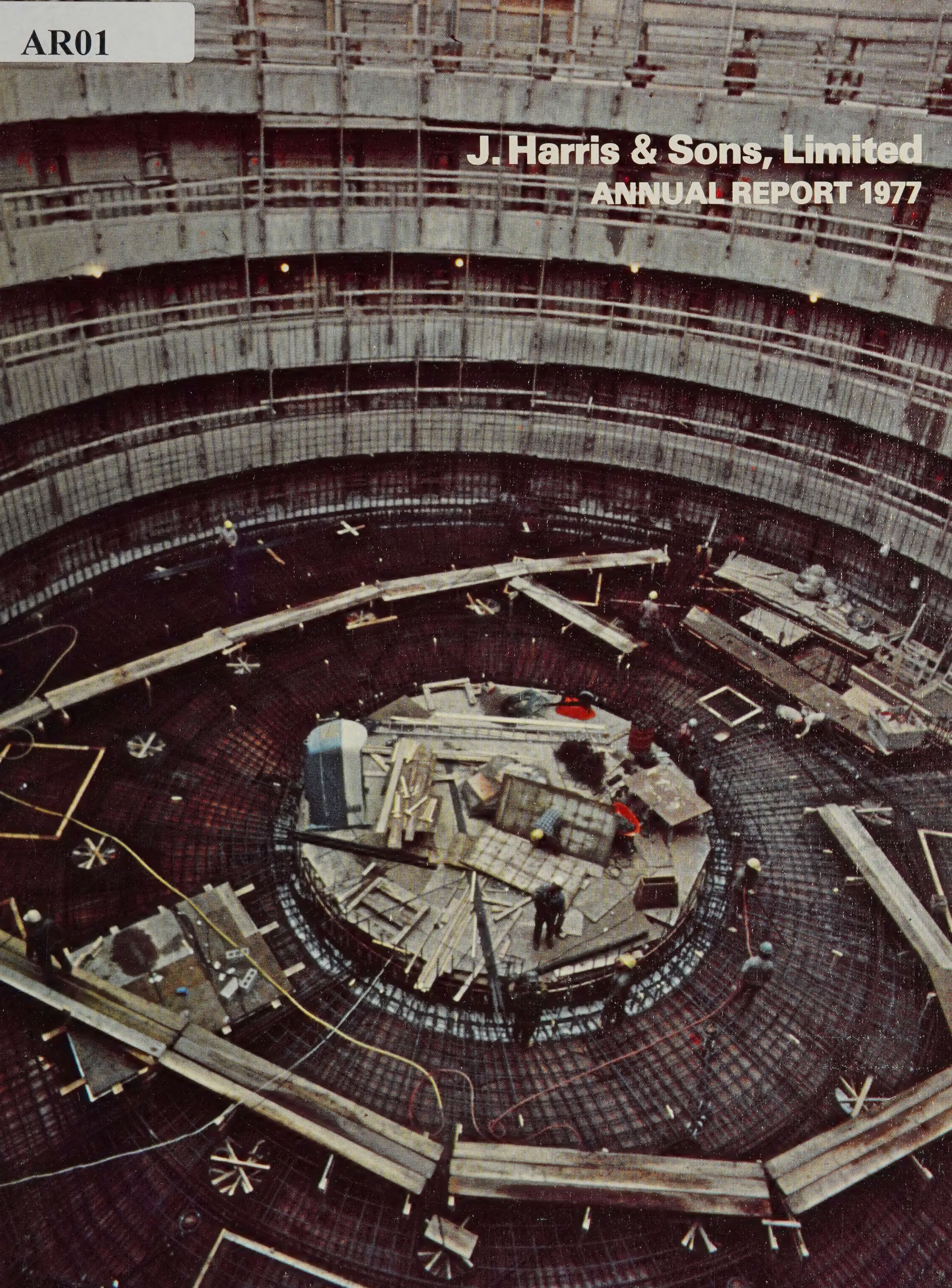
J. Harris & Sons, Limited

ANNUAL REPORT 1977



FINANCIAL HIGHLIGHTS

	1977	1976
Revenue	$55.1m	$58.6m
Net Profits	$2,848,557	$1,994,857
Per Share	$.87	$.61
Cash Flow from Operations	$3,587,220	$3,136,916
Per Share	$1.10	$.96
Working Capital	$11,891,714	$9,412,325
Shareholders Equity	$18,521,088	$16,444,441
Per Share	$5.68	$5.05
Average Shares Outstanding	3,262,875	3,256,875

OFFICERS

Milton E. Harris *Chairman & President*
James Wilson *Vice President Marketing*
Glenn Riddell *Vice President Manufacturing*
Bruce Timmerman, C.A. *Vice President Finance*
Lorie Waisberg *Secretary-Treasurer*

DIRECTORS

Gordon Atlin, Q.C. *Toronto, Ontario*
Geoffrey J. Jackson *Toronto, Ontario*
C.H. Franklin *Toronto, Ontario*
Joseph Godfrey *Toronto, Ontario*
Milton E. Harris *Toronto, Ontario*
Barrie D. Rose, C.A. *Toronto, Ontario*
Neil B. Ivory *Montreal, Quebec*

AUDITORS Clarkson Gordon & Co.

SOLICITORS Goodman and Goodman

REGISTRAR AND TRANSFER AGENT Guaranty Trust Company of Canada

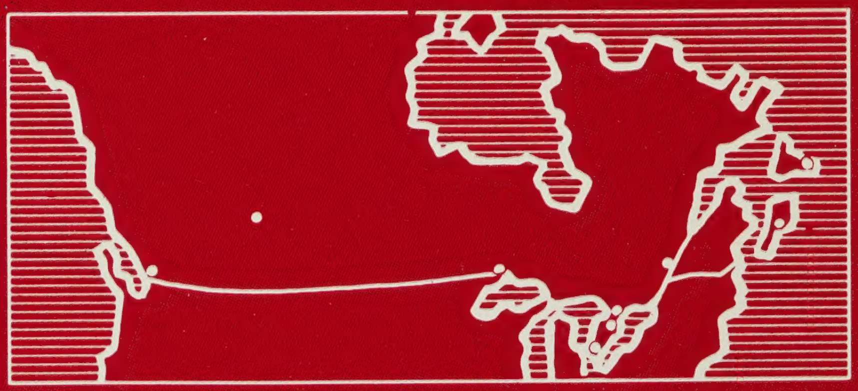
BANKERS Royal Bank of Canada
Toronto Dominion Bank

HEAD OFFICE Suite 922, 390 Bay Street, Toronto

Plants, Divisions and Subsidiary Companies

Fabrication and Supply-Reinforcing Steel	J. Harris & Sons, Limited
Fabrication, Supply and Erection-Structural Steel	Frankel Structural Steel Limited
Industrial Steel and Aluminum Grating	Fisher & Ludlow Limited
Saunders Form Hardware and Industrial Wire Products	Laurel Steel Products Limited
Concrete Post-tensioning and Reinforcing Steel Erection	VSL Canada Ltd. / VSL Ltee.
Construction Equipment Rentals	Frankel Steel Construction Services Limited
Corporate Development	J. Harris & Sons Developments (Middlesex) Limited

Offices and/or plants are located in Vancouver, Edmonton, Toronto, Milton, Burlington Stoney Creek (Hamilton), Windsor, London, Thunder Bay Montreal, Halifax, and in St. John's, Newfoundland



FRONT COVER
Work underway by J. Harris/VSL Canada at the new Metro Toronto Easterly Filtration Plant.

Report to Shareholders

We are pleased to be able to present a strong financial statement to the shareholders again this year.

We are particularly proud of our results when compared to the generally negative environment which prevailed in the steel and capital goods industry in 1977. New spending intentions for capital investment continued their downward trend under the combined influence of under-utilization of productive capacity, and the high cost of capital construction. As well, the world steel industry suffered from substantial over-supply. This caused lower steel prices and intense price competition of imports into the U.S. and Canadian markets.

1977 Was a Year of Challenge

The shortfall in demand in 1977 for most of our products caused severe competition and unrealistic pricing in many of our product lines and market areas. This tested to the utmost management's ability to seek out profit opportunities. The quality of our management team is best measured by the 20% increase in profits achieved in 1977. On behalf of the Board of Directors and the shareholders, I would like to thank our management and employees for a job well done in the face of great difficulties.

Our company has decided to abandon the joist program which we undertook three years ago. We were not able to reduce the very high cost of manufacture required by the new joist concept. Joist operating losses were about $.04 per share in 1977. A further write down of $.05 per share was taken at year end to provide for expected losses on the disposal of joist equipment.

The sale of Frankel's Shaw Street property to the City of Toronto was completed in 1977 and added $.18 per share to our equity. When the expansion of the Milton plant is completed in 1978 Frankel's total structural steel operations will be in a single, ultra-modern automated plant. Our 30-acre industrial site at Milton will accommodate major expansion in the future. Although it can be expected that we will experience additional moving and start-up costs, we anticipate significant cost reductions in the next few years.

It should be mentioned that Frankel suffered a strike of six weeks in the fall of 1977. We encountered great difficulty in explaining to the Frankel employees that market conditions could no longer support the very large settlements of the past few labour contracts. I am pleased to report that the strike was concluded on terms that will allow Frankel and its employees to continue to obtain work in a very competitive market.

Business Organization Is Effective

Our companies are organized into three management and planning groups.

The original Harris group is composed of Harris, Laurel and VSL, and operates from Stoney Creek, Ontario. The second group of companies, roughly the same size as the first, is the Frankel group, which fabricates and erects structural steel, and which we acquired in 1974. The third group is Fisher & Ludlow, acquired March 15, 1977, which manufactures heavy steel gratings at its Burlington, Ontario, plant. This was a strong company with good market position. We were able to exceed its budgeted profits for 1977. Fisher & Ludlow is now operating very effectively with a much lower overhead burden than when it was acquired.

The success of this company is further confirmation of our policy of carefully selecting acquisitions so that they fit comfortably into our overall corporate philosophy and area of expertise.

1978 Will See Healthy Steel Markets

In our opinion, the steel market we are facing in 1978 and beyond has fundamentally changed for the better. A number of new elements have combined to change the outlook for the steel industry in North America, and especially in Canada. The radical realignment of European and Japanese currencies in relation to the U.S. and Canadian dollar has reduced the ability of the major overseas steel producers to compete in the U.S. and Canada. Government policy in the U.S. through a trigger price mechanism and in Canada by anti-dumping actions and a system to monitor all steel imports have made it much more difficult to import steel into our two countries. The combination of Canadian dollar devaluation, significantly lower Canadian steel selling prices in relation to American, and low U.S. tariffs on most steel items have opened up the vast American market to the comparatively small Canadian steel industry.

These fundamental changes in the steel markets are affording our companies enormous opportunities in the marketing of our steel products.

Harris Market Opportunities Are Excellent

We are in an excellent position to take advantage of opportunities in the West and to participate in the energy construction boom which is now imminent. Harris has expanded very rapidly in Alberta out of our new Edmonton plant, Frankel was the successful bidder on a major Alberta hospital project, and Fisher & Ludlow are about to open a new fabrication plant in Calgary. I am sure you were pleased to read that Frankel, in joint venture with Canron, was just awarded one of the largest structural contracts in Canadian history for the Ontario Hydro Bruce B Nuclear Generating Station. We believe that there will be several large tender calls for electric power construction in the next few years.

Strong Balance Sheet Indicates Our Strategy

With no debt and an $18.5-million equity, we believe that we can considerably expand our corporate group, primarily utilizing unused debt facilities and thereby increasing the return on equity for our shareholders.

We expect to continue our internal expansion, and have made the capital appropriation to add two major new product lines this year and are assessing several other promising possibilities.

We continue to aggressively pursue a program of acquisition, and have redefined the duties of one of the management staff to that of full-time corporate development. Many acquisition prospects are being shown to us and some look interesting.

We will continue our successful policy of carefully selecting companies and people which are "a comfortable fit" with our corporate philosophy and expertise.

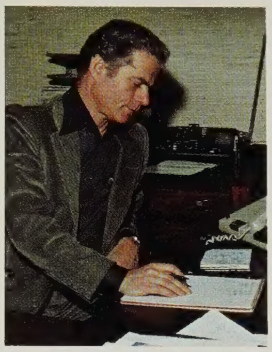
Although we continue to be interested in U.S. situations, it is our present belief that the most outstanding opportunities are in the Canadian Steel Industry.

One of the rewards of managing a successful company in an industry such as ours is the loyalty of our shareholders and, for that, we thank you all.

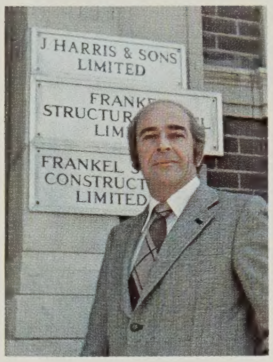
M.E. Harris

Milton E. Harris
President & Chief Executive Officer

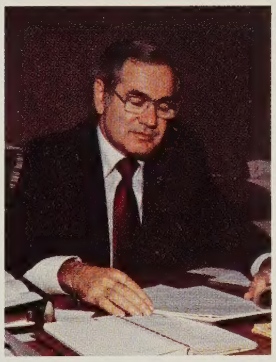
Directors of J. Harris & Sons, Limited



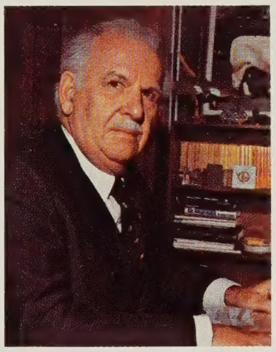
Milton E. Harris
President and Chairman of the board



Geoffrey J. Jackson
President, Frankel Structural Steel Limited



Gordon Atlin, Q.C.
Senior partner with the law firm of Atlin, Goldenberg, Cohen & Armel



Cecil H. Franklin
Chairman and Chief Executive Officer of Algonquin Mercantile Corporation; Chairman of the Board, Hardee Farms International Limited

Barrie D. Rose, C.A.
Chairman and Chief Executive Officer of Androck Company Limited

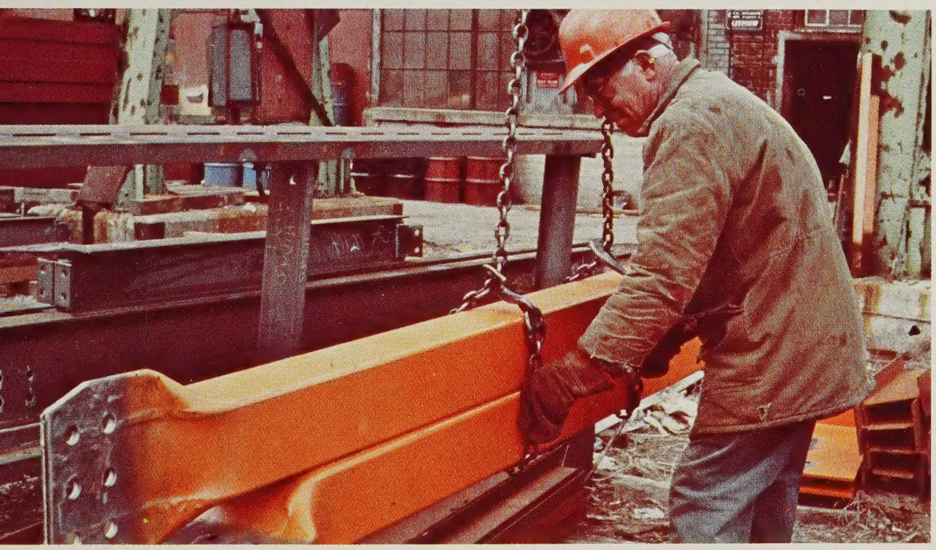
Joseph Godfrey
President and Director of York Wood Investments Limited; Jonat Construction Company Limited and Joseph Godfrey Investments Limited

Neil B. Ivory
President of Pembroke Management Ltd.; President of the Yukon Consolidated Gold Corporation Ltd.; Vice President of GBC Capital Ltd.

"We will continue our successful policy of carefully selecting companies which are 'a comfortable fit' with our corporate philosophy and expertise . . .

It is our present belief that the most outstanding opportunities are in the Canadian Steel Industry."

Activities of Harris Group employees include shop fabrication and field installation of structural steel, grating, rebars and post tensioning. In-house computer facilities aid production and management controls.



"We are in an excellent position to take advantage of opportunities in the West and to participate in the energy construction boom that is now imminent."

COMMONWEALTH STADIUM
The Commonwealth Games Stadium in Edmonton with its striking architecture was one of many major projects undertaken by J. Harris/VSL Canada during 1977.

ONTARIO HYDRO
Overview of the Nuclear Generating Station site at Douglas Point in the Bruce Peninsula. Frankel Steel, in association with Canron, was recently awarded a contract to supply and install 41,000 tons of structural steel for Phase B of Ontario Hydro's Nuclear Generating Station. Frankel/Canron completed Phase A of the program in 1977.

J. HARRIS & SONS, LIMITED
(Incorporated under the laws of Ontario)
and its subsidiary companies

CONSOLIDATED BALANCE SHEET

DECEMBER 31, 1977
(with comparative figures at December 31, 1976)

ASSETS

	1977	1976
Current:		
Short-term deposits	$1,400,000	
Accounts receivable	9,641,919	$12,713,680
Due from joint ventures	238,920	557,476
Inventories (note 2)	6,897,164	7,095,896
Estimated value of jobs in progress less progress billings	4,313,505	3,386,959
Income taxes recoverable		1,377,304
Prepaid expenses and deposits	166,057	112,809
Total current assets	22,657,565	25,244,124
Investments:		
Shares in other companies, at cost (estimated market value 1977 — $175,000; 1976 — $155,000)	44,259	44,259
Fixed assets, at cost:		
Land	763,801	2,228,770
Buildings	3,214,621	2,577,955
Machinery and equipment	11,285,242	9,612,661
	15,263,664	14,419,386
Less accumulated depreciation	7,194,444	6,465,165
	8,069,220	7,954,221
	$30,771,044	$33,242,604

AUDITORS' REPORT

To the shareholders of J. Harris & Sons, Limited:

We have examined the consolidated balance sheet of J. Harris & Sons Limited as at December 31, 1977 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of the company as at December 31, 1977, and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
April 12, 1978

Clarkson Gordon & Co.
Chartered Accountants

(See attached notes)

LIABILITIES

	1977	1976
Current:		
Bank indebtedness (inventories and accounts receivable pledged as security)	$ 1,353,970	$ 7,916,598
Accounts payable and accrued charges	5,769,833	4,607,756
Income and other taxes payable	1,218,507	891,277
Deferred income taxes — current portion	2,420,300	2,413,200
Current portion of long-term debt	3,241	2,968
Total current liabilities	10,765,851	15,831,799
Long-term debt:		
9% mortgage loan due September, 1988	61,346	64,313
Less current portion	3,241	2,968
	58,105	61,345
Deferred income taxes	1,426,000	905,019
Shareholders' equity (note 5):		
Capital (without par value) —		
Authorized:		
5,000,000 Class A shares		
5,000,000 Class B shares		
100 common shares		
Issued:		
1,006,947 Class A shares	732,891	732,891
2,258,428 Class B shares	1,724,341	1,718,341
Retained earnings	16,063,856	13,993,209
	18,521,088	16,444,441
	$30,771,044	$33,242,604

On behalf of the Board:

Director

Director

CONSOLIDATED STATEMENT OF INCOME

YEAR ENDED DECEMBER 31, 1977
(with comparative figures for 1976)

	1977	1976
Sales and construction revenue	$55,119,937	$59,051,730
Income before the following	$ 4,694,287	$ 4,948,961
Deduct:		
Depreciation	704,502	845,559
Interest on long-term debt	5,564	5,791
Other interest expense	178,118	591,754
	888,184	1,443,104
Income before income taxes and extraordinary items	3,806,103	3,505,857
Income taxes	1,374,000	1,511,000
Income before extraordinary items	2,432,103	1,994,857
Extraordinary items:		
Gain on sale of land and buildings (net of applicable taxes of $287,900)	591,463	
Provision for loss on disposal of joist division (net of applicable taxes of $127,000)	(175,009)	
	416,454	
Net income for the year	$ 2,848,557	$ 1,994,857
Earnings per share (note):		
Income before extraordinary items	$0.75	$0.61
Net income for the year	$0.87	$0.61

Note: The earnings per share are based upon the weighted average number of shares outstanding during the year. The exercise of the options referred to in note 5 would not result in any material dilution of earnings per share. (See attached notes)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	1977	1976
Source of funds:		
Income before extraordinary items	$ 2,432,103	$1,994,857
Charges to operations not involving an outlay of funds —		
Depreciation	704,502	845,559
Deferred income taxes	445,519	296,500
Loss on disposal of fixed assets	5,096	
Funds derived from operations	3,587,220	3,136,916
Proceeds from sale of fixed assets (net of current taxes of $141,000)	2,875,772	
Proceeds from the issuance of shares	6,000	6,000
	6,468,992	3,142,916
Application of funds:		
Additions to fixed assets	1,454,704	1,938,529
Dividends and special taxes related thereto	777,910	760,456
Reduction of long-term debt — non-current portion	3,240	2,968
Acquisition of subsidiary company including working capital deficiency of $932,430 assumed at the date of acquisition (note 4)	1,753,749	
	3,989,603	2,701,953
Increase in working capital	2,479,389	440,963
Working capital, beginning of year	9,412,325	8,971,362
Working capital, end of year	$11,891,714	$9,412,325

(See attached notes)

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

YEAR ENDED DECEMBER 31, 1977
(with comparative figures for 1976)

	1977	1976
Retained earnings, beginning of year	$13,993,209	$12,758,808
Net income for the year	2,848,557	1,994,857
	16,841,766	14,753,665
Deduct:		
Taxable dividends declared during year	241,437	58,471
Tax-deferred dividends declared during year	521,473	604,834
Special taxes paid by company relating to tax-deferred dividends	15,000	97,151
	777,910	760,456
Retained earnings, end of year (See attached notes)	$16,063,856	$13,993,209

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. **Accounting policies**

Basis of consolidation —

The consolidated financial statements include the accounts of the company and all its subsidiaries. Investments in joint ventures are carried at cost plus the company's share of undistributed profits to date.

Uncompleted contracts —

Estimated value of jobs in progress represents contracts in progress valued on the percentage-of-completion basis. Under the percentage-of-completion method, revenue is accrued as the work is performed, and provision is made for total anticipated losses where the estimate of total costs on a contract indicates a loss. Although the company uses its best engineering estimates, the final results of jobs in progress will necessarily be dependent upon future costs and revenues.

Inventories —

The company values its inventory at the lower of cost and market. Cost is determined on a first-in, first-out basis.

Fixed assets —

The company depreciates its buildings, machinery and equipment on a straight-line basis and its mobile equipment on a declining balance basis at the following rates:

Buildings	2½%
Machinery and equipment	7½%
Mobile equipment	30%

Gain or loss on disposal of individual assets is recognized in income in the year of disposal.

Income taxes —

The company follows the income tax allocation method of accounting. The deferred income taxes included in current liabilities relate to jobs in progress, investment in joint ventures and holdbacks receivable. Non-current deferred income taxes relate to fixed assets. The provision for income taxes is reduced by the 3% inventory allowance and the investment tax credit.

2. **Inventories**

Inventories consist of the following:

	1977	1976
Raw materials	$6,073,859	$6,558,427
Work in progress	162,644	85,319
Finished goods	660,661	452,150
	$6,897,164	$7,095,896

3. **Change in depreciation rates**

Following a review of the estimated remaining lives of the company's fixed assets, the depreciation rates on various fixed asset categories have been reduced. These adjustments as they relate to fixed assets on hand at the beginning of the year have the effect of reducing depreciation in 1977 by approximately $258,000.

4. **Acquisition of subsidiary**

On March 15, 1977, the company acquired 100% of the outstanding common and preferred shares of Fisher and Ludlow Limited in exchange for cash consideration of $821,319. This transaction was accounted for as a purchase with the operating results of Fisher and Ludlow Limited being included in the consolidated statement of earnings from the effective date of the acquisition. Net assets acquired were as follows:

Property, plant and equipment at fair value	$1,807,249
Deferred income taxes	53,500
	1,753,749
Less working capital deficiency assumed	932,430
Purchase price	$ 821,319

5. **Capital stock and dividends**

Class A and Class B shares are convertible into one another on a share-for-share basis at any time. The shares of each class rank equally in all respects, except that dividends on Class B shares may be declared payable out of the company's tax-paid undistributed surplus on hand or 1971 capital surplus on hand as defined by the Income Tax Act of Canada.

At December 31, 1977, approximately $3,051,406 of consolidated retained earnings (including approximately $1,300,000 of 1971 capital surplus) was available for the payment of tax-deferred dividends. The provision in the Income Tax Act permitting tax-deferred dividends expires December 31, 1978.

During the year under an employee stock option plan, 6,000 shares were issued for a cash consideration of $6,000.

Options are outstanding at December 31, 1977 for 12,000 shares at $1.00 per share which may be exercised to June 30, 1979 at the rate of 6,000 shares per year.

6. **Subsequent event**

On January 6, 1978, the directors authorized the proposed purchases by the company of up to 160,000 of the Corporation's class A and Class B shares on the open market, as well as the purchases of up to 100,000 Class A and Class B shares from former employees. The purchases began on January 16, 1978 and are to be concluded by June 30, 1978. To April 12, 1978 the company had acquired 81,943 Class A shares on the open market and 80,000 Class B shares from former employees for a total price (including expenses) of $672,550.

7. **Remuneration of directors and senior officers**

Remuneration of directors and senior officers of the company as defined by The Ontario Business Corporations Act, including profit sharing bonuses, amounted to $332,120 (including $7,500 as directors' fees) in 1977 and $331,885 (including $7,500 as directors' fees) in 1976.

8. **Commitments**

The company is committed to acquire plant and equipment of approximately $2,000,000 in 1978.

9. **Anti-Inflation legislation**

The company and its subsidiaries are subject to the Anti-Inflation Legislation enacted by the Government of Canada effective October 14, 1975 to provide for the restraint of profit margins, prices, employee compensation and dividends. Management is of the opinion that it is in compliance with the requirements of the Anti-Inflation legislation.

10. **Contingent liability**

A subsidiary of the company, along with a number of other defendants, has been sued for allegedly defective structural work. While the total claim for damages against all defendants is approximately $1.1 million, it is the opinion of management, based on discussions with the company's solicitors, that the ultimate liability to the company, if any, will not be significant.

J. HARRIS & SONS, LIMITED

FINANCIAL SUMMARY

	1977	1976	1975	1974	1973
Revenue	$55.1m	$58.6m	55.2m	40.9m	20.4m
Profits	$2.8m	$2.0m	4.9m	5.8m	1.3m
Per Share (A)	87¢	61¢	$1.50	$2.12	49¢
Funds Provided	$3.6m	$3.1m	5.8m	6.3m	1.6m
Per Share (A)	$1.10	96¢	$1.78	$2.28	60¢
Dividends (A)	23.4¢	20.4¢	16¢	10.2¢	4¢
Effective Tax Rate (including deferred)	36%	43%	45%	45%	46%
Financial:					
Assets	$30.8m	$33.2m	29.2m	29.5m	8.3m
Long-term debt	$61,346	$64,313	67,031	5,154,960	697,368
Current Assets	$22,657,565	$25,244,124	22,259,447	23,800,482	6,894,021
Current Liabilities	$10,765,851	$15,831,799	13,288,085	13,915,964	4,127,654
Working Capital	$11,891,714	$9,412,325	8,971,362	9,884,518	2,766,367
Current Ratio	2.1:1	1.6:1	1.7:1	1.7:1	1.7:1
% Inventory to Current Assets	49%	42%	43%	44%	34%
Capitalization:					
Common Shares	$2,457,232	$2,451,232	2,445,232	2,445,232	411,214
Retained earnings	$16,063,856	$13,993,209	12,758,808	8,458,896	2,955,968
Shareholders Equity	$18,521,088	$16,444,441	15,204,040	10,904,128	3,367,182
Per Share (A)	$5.68	$5.05	$4.67	$3.97	$1.25

A — Based on average number of shares outstanding after 3 for 1 split in 1974.